

# Ratcheting Up the Duty: The Department of Labor’s Misguided Attempt To Impose a Paternalistic Model upon Defined Contribution Plans Through ERISA

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## I. INTRODUCTION

“A penny saved is a penny earned”<sup>1</sup> is a proverb that most young students of American History would recognize. From childhood, we are often taught that saving income for future needs is a virtue. The financial education of children seems to be a topic on which we can all agree. For example, *Sesame Street* and PNC Bank recently joined forces to teach finance fundamentals in a multimedia campaign.<sup>2</sup> However, at some point, the message becomes lost. While Social Security provides up to forty percent of an average earner’s income after retirement,<sup>3</sup> and may keep some Americans out of poverty in old age, Social Security cannot alone provide sufficient retirement security.<sup>4</sup> According to a 2012 report, baby-boomers and Gen X-ers are not saving enough.<sup>5</sup> Fifty-six percent of workers concede they have not even calculated how much they will need for retirement.<sup>6</sup>

Since the 1940s, pension plans have become an important factor in the average American worker’s general welfare.<sup>7</sup> ERISA was enacted to improve retirement security through regulation of employees’ pension plans. Through litigation, proposed regulatory changes, and guidance updates, the Department of Labor has recently attempted to further ERISA’s goal by increasing the

<sup>1</sup> The quotation is commonly attributed to Ben Franklin, but is in fact of Scottish origin. Edward J. McCaffery, *Tax Policy Under a Hybrid Income-Consumption Tax*, 70 TEX. L. REV. 1145, 1163 n.87 (1992).

<sup>2</sup> Eileen Aj Connelly, *Sesame Street, PNC Bank Team Up To Teach Kids About Money*, USA TODAY (Apr. 19, 2011, 10:12 AM), <http://usatoday30.usatoday.com/money/perfi/general/2011-04-17-finance-education.htm>.

<sup>3</sup> SOC. SEC. ADMIN., SSA PUB. NO. 05-10024, UNDERSTANDING THE BENEFITS 4 (2014), available at <http://www.ssa.gov/pubs/10024.html#a0=0>.

<sup>4</sup> It is understood that comfortable living after retirement requires replacement of seventy percent of prior income—more than forty percent. *Id.*

<sup>5</sup> These groups are currently facing a \$4.3 trillion retirement income deficit. Sheyna Steiner, *Retirement Savings Improve, but Not Enough*, CNBC (Aug. 22, 2012, 9:45 AM), [http://www.cnbc.com/id/48749880/Retirement\\_Savings\\_Improve\\_but\\_Not\\_Enough](http://www.cnbc.com/id/48749880/Retirement_Savings_Improve_but_Not_Enough).

<sup>6</sup> Calculating retirement income needs is the first step toward successful retirement planning. Without a goal in mind, individuals cannot know how much to save and invest every year to reach an adequate amount of funds upon retirement. *Id.*

<sup>7</sup> H.R. REP. NO. 93-533, pt. 2, at 2 (1973). Pension plans have been identified as one of three pillars of retirement security, in addition to Social Security and personal savings. Chase A. Tweel, *Retirement Savings in the Face of Increasing Longevity: The Advantages of Deferring Retirement*, 14 N.C. BANKING INST. 103, 104 (2010).

fiduciary duty of directed trustees, service providers, and employers.<sup>8</sup> The idea being, if the fiduciary duty attendant to servicing and providing pension plans was to increase, employers and pension service providers would be held accountable for investment losses in the plans.<sup>9</sup> At the same time, the threat of becoming accountable for losses will motivate these actors to provide less varied, more paternalistic plan designs to employees or cease offering them altogether, as the liability potential increases.<sup>10</sup> The Department of Labor seems to believe that employees cannot make investment decisions for themselves. ERISA does not require employers to offer employee benefit plans, so employers may choose to stop supplying them altogether, thus eliminating an important source of retirement security.

The Department of Labor should instead focus on the goal of retirement security by empowering employees to make informed decisions and decreasing fiduciary responsibilities appurtenant to efforts to meet this goal. By focusing on creating the proper incentives to educate employees, the Department of Labor will allow trustees, investment advisers, and employers to build off of values acquired by employees in earlier years of life, such as saving for future needs.

This Note contends that the Department of Labor's efforts to heighten the fiduciary duties of those providing and administering defined contribution plans under ERISA will not accomplish increased retirement security. Part II describes the history of the enactment of ERISA and describes its original fiduciary standard, as well as the rise of defined contribution plans. The history illustrates that Congress did not intend to impart relatively high levels of fiduciary duty in almost every situation, because it could have done so in the statute and did not. Part III examines the Department of Labor's recent efforts to alter the law of directed trustees, broaden the definition of fiduciary to include many service providers, and impose new obligations upon plans' sponsors where the plan includes open brokerage window features. Although they did not meet with much success, there is a concerted effort to ratchet up fiduciary duty through these actions. Part IV argues that the Department of Labor's recent actions conform to a paternalistic model because they have the impact of limiting employees' options. The Department will not increase retirement security by any measure because the financial industry would rather cease offering services than be subjected to the risk of accounting for employees' losses and other sanctions under ERISA. Part V proposes that the Department of Labor should redirect its efforts toward providing employees with the knowledge to make safe investment decisions themselves.

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<sup>8</sup> See *infra* Part III.

<sup>9</sup> See *infra* notes 42–46.

<sup>10</sup> See *infra* notes 88–89, 98–99, 114–15.

## II. OVERVIEW OF ERISA AND GROWTH OF DEFINED CONTRIBUTION PLANS

### A. *The Purpose of ERISA Is Retirement Security*

The Employee Retirement Income Security Act of 1974, as amended (ERISA or the Act) has often been called a “comprehensive and reticulated statute.”<sup>11</sup> While its form may be complicated, its purpose is clear: ERISA was enacted to further the purpose of helping to provide retirement security for employees. In 1974, Congress found it necessary to establish minimum standards to assure the “financial soundness” and equitable nature of employee benefit plans to ensure benefits would be paid as promised.<sup>12</sup> American workers had a right to look forward to a retirement with “financial security and dignity.”<sup>13</sup> In signing the bill into law, President Ford promised that ERISA would help to provide that retirement dollars would be available to employees “when they are needed.”<sup>14</sup>

Two key historical events leading to the enactment of ERISA illustrate the problem as Congress saw it at the time. First, in 1963, the Studebaker-Packard Corporation closed a plant in South Bend, Indiana.<sup>15</sup> At the time, the company’s pension plans were so underfunded that only those workers over sixty years of age received the full value of their pensions, while others received only fifteen percent or nothing.<sup>16</sup> Second, in 1972, the National Broadcasting Corporation aired an exposé that detailed significant injustices in the private pension system, broadcasting the issue to the American public.<sup>17</sup> The documentary detailed stories of destitute individuals who were promised pensions upon retirement that they ultimately never received due to various unfair methods of plan

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<sup>11</sup> *Great-West Life & Annuity Ins. Co. v. Knudson*, 534 U.S. 204, 209 (2002); *Mass. Mut. Life Ins. Co. v. Russell*, 473 U.S. 134, 146 (1985) (stating that the ERISA remedial scheme is “interlocking, interrelated, and interdependent”); *Nachman Corp. v. Pension Benefit Guar. Corp.*, 446 U.S. 359, 361 (1980).

<sup>12</sup> 29 U.S.C. § 1001(a) (2012). Before the enactment of ERISA, employees could lose their retirement benefits within days of qualifying for retirement, even if the plan had already vested. See H.R. REP. NO. 93-533, pt. 2, at 5.

<sup>13</sup> H.R. REP. NO. 93-533, pt. 5, at 8 (1973).

<sup>14</sup> *President Ford Signing ERISA of 1974*, PENSION BENEFIT GUARANTY CORP., <http://www.pb.gc.gov/about/who-we-are/pg/president-ford-signing-erisa-of-1974.html> (last visited Apr. 2, 2014).

<sup>15</sup> James A. Wooten, “*The Most Glorious Story of Failure in the Business*”: *The Studebaker-Packard Corporation and the Origins of ERISA*, 49 BUFF. L. REV. 683, 683 (2001).

<sup>16</sup> *Id.* at 731. This event helped push legislative debate about pensions into the public arena. *Id.* at 684.

<sup>17</sup> *Pensions: The Broken Promise* (NBC television broadcast Sept. 12, 1972), available at <http://archives.nbclearn.com/portal/site/k-12/flatview?cuecard=57200>.

operation.<sup>18</sup> The program raised public support for employee benefit program reform to its highest level. Congress soon held hearings on the issue, and the enactment of ERISA then followed.<sup>19</sup>

Although ERISA does not require employers to create employee benefit plans or keep them indefinitely,<sup>20</sup> it does regulate private employee pension plans comprehensively.<sup>21</sup> ERISA's various reporting and disclosure requirements, for example, require all plans to be in writing and in a "manner calculated to be understood by the average plan participant."<sup>22</sup> In terms of equitable plan operation, ERISA requires minimum vesting standards, minimum funding of pension plans, and provides a fiduciary standard for those exercising discretionary authority in managing a plan.<sup>23</sup> ERISA also amended the Internal Revenue Code, providing certain favorable tax treatment for the establishment or maintenance of pension plans under the Act, thus providing an incentive for employers to establish plans.<sup>24</sup> The Act provides for enforcement of its provisions both in the civil and criminal realms.<sup>25</sup> Employees seeking redress for violations of ERISA provisions that have negatively affected them

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<sup>18</sup> *Id.* (stating that employers left many restrictions on receiving benefits "buried in fine print," fired employees just before they became vested in benefits, and moved employees from position to position without making their benefits portable among the positions).

<sup>19</sup> James P. Allen & Richard A. Bales, *ERISA Failures and the Erosion of Workers' Rights: The Urgent Need To Protect Private & Public Workers' Pensions and Benefits*, 75 ALB. L. REV. 449, 460–61 (2012) ("The public outcry that followed the airing of the program resulted in a series of congressional hearings on pension reform over the next five years.").

<sup>20</sup> *Curtiss-Wright Corp. v. Schoonejongen*, 514 U.S. 73, 78 (1995) ("Employers or other plan sponsors are generally free under ERISA, for any reason, at any time, to adopt, modify, or terminate welfare plans."); see *Lockheed Corp. v. Spink*, 517 U.S. 882, 890 (1996) (holding that a decision to terminate a plan does not trigger fiduciary liability because it is similar to the actions of a settlor of a trust).

<sup>21</sup> *Nachman Corp. v. Pension Benefit Guar. Corp.*, 446 U.S. 359, 375 (1980); Peter K. Stris & Victor A. O'Connell, *Enforcing ERISA*, 56 S.D. L. REV. 515, 516 (2011). ERISA also regulates employee healthcare plans, termed "employee welfare benefit plan[s]" by the Act. 29 U.S.C. § 1002(1) (2012).

<sup>22</sup> 29 U.S.C. § 1022; see also 29 U.S.C. § 1102(a)(1) ("Every employee benefit plan shall be established and maintained pursuant to a written instrument.").

<sup>23</sup> When a benefit vests, it must be provided to the employee at the specified time of distribution. See 29 U.S.C. § 1053 (providing that after a certain number of years of service, a certain portion of a participant's benefit becomes nonforfeitable). ERISA prohibits underfunding plans that require employer contributions to pay promised benefits to employees. See 29 U.S.C. § 1082(a)(1) (stating an ERISA plan "shall satisfy the minimum funding standard applicable"). ERISA's fiduciary standard is described *infra* Part II.B.

<sup>24</sup> See Leonard A. Nelson, *Aetna v. Davila/Cigna v. Calad: A Missed Opportunity*, 31 WM. MITCHELL L. REV. 843, 845 (2005) ("The purpose of ERISA is to broaden and strengthen the social safety net by encouraging employers, primarily through federal income tax preferences, to provide certain non-salary benefits to employees.").

<sup>25</sup> Criminal penalties include fines and imprisonment. 29 U.S.C. § 1131. Criminal liability requires willful or intentional misconduct, so it is imposed more rarely than civil liability. See Stris & O'Connell, *supra* note 21, at 519 n.37.

can sue to recover benefits on behalf of the plan or on behalf of themselves in equity.<sup>26</sup>

The Department of Labor has regulatory oversight authority over ERISA.<sup>27</sup> The Department has created a substantial body of law construing ERISA through its rule-making authority. It has standing to enforce ERISA to assess civil penalties<sup>28</sup> and can carry out investigations of violations that may later be prosecuted by U.S. Attorneys. The Department created the Employee Benefits Security Administration (EBSA) to administer and enforce the Department's authority over ERISA's fiduciary standard.<sup>29</sup> The EBSA issues technical guidance, including interpretive bulletins, advisory opinions, and information letters that construe ERISA and its accompanying regulations, providing an additional source of law.<sup>30</sup>

At the heart of ERISA, there exists a balance between the interests of employers and employees.<sup>31</sup> Employees benefit because their promised pension funds become nonforfeitable after vesting, and employers benefit from tax deductions on their plan contributions.<sup>32</sup> Congress's goal was to provide income security to employees, but it knew that if pension plans became too expensive,

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<sup>26</sup>Monetary damages would not be recoverable in equity. Allen & Bales, *supra* note 19, at 467 (citing Great-West Life & Annuity Ins. Co. v. Knudson, 534 U.S. 204, 219–20 (2002)). However, equity would include a court order to provide a benefit that was previously denied. COLLEEN E. MEDILL, INTRODUCTION TO EMPLOYEE BENEFITS LAW 551 (3d ed. 2011).

<sup>27</sup>The Department of Treasury has authority over ERISA's Internal Revenue Code provisions. See MEDILL, *supra* note 26, at 26, 96, 213.

<sup>28</sup>See, e.g., 29 U.S.C. § 1132(l) (2012) (stating “the Secretary shall assess a civil penalty” in the case of breach of fiduciary responsibility).

<sup>29</sup>EBSA also has authority over ERISA's disclosure and reporting provisions. *History of EBSA and ERISA*, U.S. DEP'T LABOR, <http://www.dol.gov/ebsa/aboutebsa/history.html> (last visited Jan. 7, 2014).

<sup>30</sup>MEDILL, *supra* note 26, at 26; see William R. Andersen, *Informal Agency Advice—Graphing the Critical Analysis*, 54 ADMIN. L. REV. 595, 595–97 (2002); Connor N. Raso, Note, *Strategic or Sincere? Analyzing Agency Use of Guidance Documents*, 119 YALE L.J. 782, 782–96 (2010) (discussing agency use of informal guidance documents and the weight given to them in courts).

<sup>31</sup>H.R. REP. NO. 93-533, pt. 5, at 9 (1973) (“The [ERISA] Bill reported by the Committee represents an effort to strike an appropriate balance between the interests of employers and labor organizations . . . bring[ing] the workers' interest up to parity with those of employers.”).

<sup>32</sup>Employers may deduct amounts contributed to qualified pension plans, although employees do not claim those amounts as income until the benefits are distributed, usually at retirement. 26 U.S.C. § 404 (2012) (setting rules and limits for deductions). Individuals who run businesses and have the power to authorize the adoption also benefit from ERISA plans; they may set up plans that help their employees because they can enroll themselves and defer taxation on their compensation. Norman P. Stein, *An Alphabet Soup Agenda for Reform of the Internal Revenue Code and ERISA Provisions Applicable to Qualified Deferred Compensation Plans*, 56 SMU L. REV. 627, 630 (2003).

then employers would not provide them and the ultimate goal would be lost.<sup>33</sup> Policymakers need to remember that placing their thumb on the scale too strongly may cause a critical balance to topple.

### B. *The Current, Fact-Specific Definition of a Fiduciary and the Duties of a Fiduciary*

One of the central pillars of ERISA's regulatory framework is the fiduciary concept; accordingly, ERISA's fiduciary duty standard is one of the highest in the law.<sup>34</sup> The role of the fiduciary pervades almost all aspects of the employee benefit plan's function and fulfills the policy goals providing for retirement security in many ways. For instance, the role of the fiduciary begins at the beginning: every plan must be established pursuant to a written document that names a fiduciary.<sup>35</sup> This writing requirement helps to fulfill the goal of retirement security by apprising plan participants of their rights under the plan and deterring fiduciaries from misconduct, because they know participants would blame them if something were to go wrong.<sup>36</sup> Furthermore, the mandated fiduciary duties<sup>37</sup> in ERISA ensure proper plan governance, to provide that plans have "adequate funds to pay promised benefits."<sup>38</sup> For example, ERISA

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<sup>33</sup> S. REP. NO. 93-383, pt. 5, at 18 (1973) ("[T]he cost of financing pension plans is an important factor in determining whether any particular retirement plan will be adopted [and] unduly large increases in costs could impede the growth and improvement of the private retirement system. . . . [T]he committee has sought to adopt provisions which strike a balance between providing meaningful reform and keeping costs within reasonable limits."); see Brendan S. Maher, *Creating a Paternalistic Market for Legal Rules Affecting the Benefit Promise*, 2009 WIS. L. REV. 657, 665–69 (explaining that creating ERISA provisions that promote employees' interests, such as the likelihood of receiving benefits, carries a trade-off in terms of costs to employers, that may ultimately lead to benefit reduction or elimination if costs increase too highly).

<sup>34</sup> 29 U.S.C. § 1001(b) (2012) (stating it is the policy of ERISA to protect the interests of participants and their beneficiaries "by establishing standards of conduct, responsibility, and obligation for fiduciaries of employee benefit plans"); MEDILL, *supra* note 26, at 397 ("The legal duties and potential liability associated with fiduciary status . . . are significant.").

<sup>35</sup> 29 U.S.C. § 1102(a)(1). Note that failure to establish a plan with a written document will not extinguish coverage under ERISA, but would lead to liability. See *Donovan v. Dillingham*, 688 F.2d 1367, 1372 (11th Cir. 1982) ("[I]t would be incongruous for persons establishing or maintaining informal or unwritten employee benefit plans, or assuming the responsibility of safeguarding plan assets, to circumvent the Act merely because an administrator or other fiduciary failed to satisfy reporting or fiduciary standards.").

<sup>36</sup> See H.R. REP. NO. 93-533, pt. 6, at 11 ("Experience has also demonstrated a need for a more particularized form of reporting so that the individual participant knows exactly where he stands with respect to the plan . . . . [T]he safeguarding effect of the fiduciary responsibility section will operate efficiently only if fiduciaries are aware that the details of their dealings will be open to inspection . . . .").

<sup>37</sup> See 29 U.S.C. §§ 1101–1114.

<sup>38</sup> 29 U.S.C. § 1001(a).

requires fiduciaries to act with the care and diligence that a prudent person in the fiduciary's position would act<sup>39</sup> and for the exclusive benefit of plan participants.<sup>40</sup> Therefore, fiduciaries must conscientiously investigate the merits of important decisions they make.<sup>41</sup> ERISA explicitly prohibits self-dealing among fiduciaries.<sup>42</sup>

Finally, ERISA's provisions for liability for breach of fiduciary duty further ERISA's goal of effective plan management and "ready access to the Federal courts."<sup>43</sup> Fiduciaries can be held personally liable for any losses that result from their breaches.<sup>44</sup> In addition, fiduciaries can be brought to court for the breaches of other fiduciaries to the plan, which broadens the possibility of liability.<sup>45</sup> As punishment for conducting prohibited transactions, fiduciaries can be subject to punitive excise taxes, a twenty percent sanction, or be forced to restore any losses to the plan and profits resulting from the transaction.<sup>46</sup> These provisions punish conduct that could be abusive toward the administration of plans and generally reflects poorly on the goal of retirement security.<sup>47</sup>

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<sup>39</sup> 29 U.S.C. § 1104(a)(1)(B). The standard of the prudent man that ERISA utilizes developed under the common law of trusts. *MEDILL*, *supra* note 26, at 433–34.

<sup>40</sup> 29 U.S.C. § 1104(a)(1)(A). ERISA's duty of loyalty can also be traced back to common law origins. *See Freund v. Marshall & Illsey Bank*, 485 F. Supp. 629, 639 (W.D. Wis. 1979) (quoting *Meinhard v. Salmon*, 164 N.E. 545, 549 (N.Y. 1928)).

<sup>41</sup> *See Schaefer v. Ark. Med. Soc'y*, 853 F.2d 1487, 1491 (8th Cir. 1988) ("A fiduciary is obligated to investigate all decisions that will affect the pension plan.").

<sup>42</sup> 29 U.S.C. § 1106(b). ERISA also prohibits transactions between a plan and a party in interest, someone who has a connection either with the plan or the plan's sponsor, that could influence the fiduciary's decision to authorize the transaction. *MEDILL*, *supra* note 26, at 456–57. These transactions are illegal per se, so there is no need to prove in litigation that the specific transactions were detrimental to the plan. *Id.* at 437.

<sup>43</sup> 29 U.S.C. § 1001(b).

<sup>44</sup> 29 U.S.C. § 1109. The fiduciary would have to "make good" the losses (restore them) and pay back ill-gotten profits. Harvey R. Herman, *ERISA Statutory Overview and Fiduciary Duties*, CLAUSEN MILLER (Dec. 2007), [http://www.clausen.com/index.cfm/fa/firm\\_pub.article/article/57b5ebdc-113c-4f56-b753-16d63768f438/ERISA\\_Statutory\\_Overview\\_and\\_Fiduciary\\_Duties.cfm](http://www.clausen.com/index.cfm/fa/firm_pub.article/article/57b5ebdc-113c-4f56-b753-16d63768f438/ERISA_Statutory_Overview_and_Fiduciary_Duties.cfm). Someone who is held to be personally liable must satisfy judgments from his own personal assets. BLACK'S LAW DICTIONARY 702 (9th ed. 2009).

<sup>45</sup> 29 U.S.C. § 1105. This co-fiduciary liability exists only when the fiduciaries enabled the breaches through misfeasance, acted to conceal the breaches, or knew about the breach and failed to make reasonable efforts to fix the effects of the breach. *Id.*

<sup>46</sup> Prohibited transactions include self-dealing, conflicts, and other duty of loyalty issues. *MEDILL*, *supra* note 26, at 458. Similar to party in interest transactions, courts construe prohibited transactions strictly against fiduciaries. *Id.* The amount to be paid to the IRS could be as high as fifteen percent of the amount of money involved in the prohibited transaction, or all of it if the problem is not corrected. 26 U.S.C. § 4975(a)–(b) (2012).

<sup>47</sup> *See Mass. Mut. Life Ins. Co. v. Russell*, 473 U.S. 134, 142 (1985) (stating fiduciary obligations "serve the interest of participants and beneficiaries and, specifically, to provide them with the benefits authorized by the plan"); *Donovan v. Cunningham*, 716 F.2d 1455, 1465 (5th Cir. 1983) (noting that prohibited transaction rules make "illegal per se the types of transactions that experience had shown to entail a high potential for abuse").



The designation of a fiduciary, with the prospect of massive liability for breach, is important. But beyond the easily identifiable named fiduciary in a plan document, the question of who is a fiduciary is complex.<sup>48</sup> For example, a person may be regarded as a fiduciary with regard to some decisions that affect an employee benefit plan but not others.<sup>49</sup> Currently, ERISA provides a functional definition: persons can be fiduciaries if they exercise discretionary authority or control, render investment advice for a fee, or have discretionary authority or responsibility.<sup>50</sup> The Department further defined investment advice in its regulation as advice that will serve as the primary basis of investment decisions, as to the value of securities, on a regular basis, pursuant to a mutual agreement, and will be individualized with respect to the particular needs of the plan.<sup>51</sup>

In other words, people become fiduciaries based on their conduct. While the ultimate query may be fact-driven, and is bound to be “hotly contested,”<sup>52</sup> there is no reason to question Congress’s decision to not provide a more exact definition with a bright line. Courts construing ERISA have developed the definition of terms that define ERISA coverage, such as “employee”<sup>53</sup> and even “plan,”<sup>54</sup> in highly fact-specific terms that may also be hotly contested in litigation. If Congress wanted to narrowly define these terms, which are threshold questions that determine whether ERISA’s rights will be provided to a person, it could have.

### *C. Shift in Pension Landscape from Defined Benefit to Defined Contribution Plans*

ERISA specifies two types of pension plans: defined benefit and defined contribution.<sup>55</sup> A defined benefit plan provides a set amount of income to the

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<sup>48</sup> See 29 U.S.C. § 1102(a) (2012) (stating every employee benefit must be established and maintained pursuant to a written instrument that provides for “named fiduciaries”).

<sup>49</sup> *E.g.*, *Bernstein v. Metro. Life Ins. Co.*, 453 F. Supp. 2d 554, 560 (D. Conn. 2006) (stating ERISA plan administrators have a fiduciary duty to oversee a plan but not a fiduciary duty to respond to individualized requests for information); see Deborah S. Davidson & Emily A. Glunz, *ERISA Fiduciary Litigation*, in ABA JCEB 19TH ANNUAL NATIONAL INSTITUTE ON ERISA LITIGATION B-19, B-23 (Nov. 16–17, 2009).

<sup>50</sup> 29 U.S.C. § 1002(21)(A) (2012).

<sup>51</sup> 29 C.F.R. § 2510.3-21 (2013).

<sup>52</sup> MEDILL, *supra* note 26, at 399.

<sup>53</sup> *Nationwide Mut. Ins. Co. v. Darden*, 503 U.S. 318, 323–24 (1992) (applying a multi-factor common law test).

<sup>54</sup> *Donovan v. Dillingham*, 688 F.2d 1367, 1373 (11th Cir. 1982) (stating a “plan, fund, or program” is determined from the “surrounding circumstances”).

<sup>55</sup> 29 U.S.C. § 1002(34)–(35) (defining a defined contribution plan as “a pension plan which provides for an individual account for each participant and for benefits based solely upon the amount contributed to the participant’s account” and a defined benefit plan as a “plan other than an individual account plan”).

participant as a pension, perhaps as an annuity.<sup>56</sup> When the participant's accrued benefit in the defined benefit plan vests, it creates an obligation on the employer to pay the required amount upon the employee's retirement.<sup>57</sup> Therefore, the plan defines the benefit to which the participant will be entitled and the employer bears the risk of bad investments.<sup>58</sup> Some employees are further protected by the Pension Benefit Guaranty Corporation, which insures defined benefit plans in the event of certain corporate events, such as bankruptcy.<sup>59</sup>

On the other hand, defined contribution plans are funded by the contributions of either an employer or employee into an account individualized for the employee and the earnings on these contributions.<sup>60</sup> When employees with defined contribution plans retire, they receive the full value of their account.<sup>61</sup> The defined contribution plan does not guarantee any specific amount or benefit; rather, the amount of the distribution depends on the amount contributed to the plan and the growth of the assets in the plan.<sup>62</sup> Another distinctive feature of defined contribution plans, such as the 401(k) salary deferral contribution plan, is the employee's control over how much to contribute<sup>63</sup> and where to invest the funds.<sup>64</sup> This feature is critical: employees with defined contribution plans bear the risk of their investment choices failing, so they must make these choices diligently.

When ERISA was adopted, most plans fell under the defined benefit framework.<sup>65</sup> Now, however, most pension plans under ERISA are defined

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<sup>56</sup> Edward A. Zelinsky, *The Defined Contribution Paradigm*, 114 YALE L.J. 451, 456 (2004).

<sup>57</sup> *Id.* (“[T]raditional defined benefit plans are funded collectively, the employer's contributions being pooled in a common trust fund . . . . If the funds in the trust are inadequate to pay promised benefits, the employer is obligated to make up the shortfall.”).

<sup>58</sup> Risk referring to the question of whether or not there will be sufficient assets to fund distributions to participants.

<sup>59</sup> 29 U.S.C. § 1302(a)(2) (2012) (establishing the Pension Benefit Guaranty Corporation to “provide for the timely and uninterrupted payment of pension benefits to participants and beneficiaries”); see Zelinsky, *supra* note 56, at 477 (stating the Pension Benefit Guaranty Corporation “resembles the FDIC”).

<sup>60</sup> *LaRue v. DeWolff, Boberg & Assocs., Inc.*, 552 U.S. 248, 250 n.1 (2008) (stating the value of a defined contribution account is “a function of the amounts contributed to that account and the investment performance of those contributions”).

<sup>61</sup> Susan J. Stabile, *Paternalism Isn't Always a Dirty Word: Can the Law Better Protect Defined Contribution Plan Participants?*, 5 EMP. RTS. & EMP. POL'Y J. 491, 494 (2001).

<sup>62</sup> MEDILL, *supra* note 26, at 114.

<sup>63</sup> Within certain limits that the Internal Revenue Code imposes. The limits can be changed yearly to account for inflation. See I.R.S. News Release IR-2012-77 (Oct. 18, 2012), available at <http://www.irs.gov/uac/2013-Pension-Plan-Limitations>.

<sup>64</sup> Colleen E. Medill, *The Individual Responsibility Model of Retirement Plans Today: Conforming ERISA Policy to Reality*, 49 EMORY L.J. 1, 11 (2000).

<sup>65</sup> Stabile, *supra* note 61, at 498 (stating that ERISA was drafted with defined benefit plans in mind).

contribution plans.<sup>66</sup> One reason for the shift is the relative expense of defined benefit plans.<sup>67</sup> Also, some defined contribution plans are more portable than defined benefit plans in a work environment where employees can expect to work for many employers, rather than perform as a “company man” through their careers.<sup>68</sup>

The Department’s attempts to broaden fiduciary duty<sup>69</sup> affect defined contribution plans and involve an effort to rein in their distinctive feature: participant direction over investments. That effort is paternalistic by nature. But fiduciary duty in ERISA is already broad and Congress intended its coverage to be fact specific, not so wide as to intrude upon participant direction.<sup>70</sup> The Department, if it could succeed in the goal implied by its proposed changes, would also increase the cost of providing pension plans. To the extent the increased cost would cause employers to abandon their plans, the balance at the heart of ERISA and the goal of retirement security for Americans would be harmed. A superior course of action for the Department would involve acknowledgment of the role of participant direction and would help employers educate their employees to make prudent choices with their defined contribution plans.<sup>71</sup>

### III. DEPARTMENT OF LABOR’S ATTEMPTS TO RATCHET UP FIDUCIARY DUTY UNDER ERISA

The Department of Labor is trying to alter the balance of ERISA. This Part details attempts by the Department to widen the fiduciary duties of those who offer services to participants exercising their direction, or choice, over investments in defined contribution plans. The point is not to criticize specific proposed changes of ERISA, but rather to illustrate a pattern. In a broad sense, this process could have the impact of further decreasing the level of participant direction over retirement plan accounts, a goal that is paternalistic because it assumes participants cannot navigate these choices. With increased fiduciary duty comes increased potential for liability and increased costs to provide

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<sup>66</sup> Salvatore J. Papa, *The Current Crisis of I.R.C. § 401(k): Is Providing Investment Advice the Proper Solution? The Misguided Focus on Investment Advice Instead of Investment Education*, 38 NEW ENG. L. REV. 371, 378 (2004). There are over 500,000 participant-directed individual account plans. EMP. BENEFITS SEC. ADMIN., U.S. DEP’T OF LABOR, FACT SHEET, DEFINITION OF THE TERM “FIDUCIARY” 1 (2011).

<sup>67</sup> Stabile, *supra* note 61, at 496–97 (stating that defined benefit plans are more costly and more regulated than defined contribution plans).

<sup>68</sup> See Zelinsky, *supra* note 56, at 473–75 (arguing that as the usefulness of rollover account features increased when employees began to switch jobs more, the individual account system of defined contribution plans became more popular).

<sup>69</sup> See discussion *infra* Part III.

<sup>70</sup> See *supra* Part II.B.

<sup>71</sup> Some possible solutions are listed *infra* Part V.

services.<sup>72</sup> By increasing fiduciary duties, many actors and programs that facilitate participant direction may be reined in or forced to retire altogether. The Department's proposed changes have largely not been enacted, but the reelection of President Obama may embolden it—or other agencies—to continue on its current path.<sup>73</sup>

### *A. Directed Trustees Must Question Purchases of Employer Stock*

The Department has attempted to broaden the duties of ERISA-directed trustees, widening the scope of potential liability for ERISA violations. By default, ERISA requires that assets in a plan be held in a trust, subject to the control of a trustee.<sup>74</sup> While the employer sponsoring the plan can act as the plan's trustee, named fiduciaries can also appoint directed trustees to control plan assets.<sup>75</sup> These directed trustees could be banks, trust companies, or stock brokerage companies.<sup>76</sup> Directed trustees must follow the directions given to them, but these directions must be proper: the directions cannot contradict the requirements of ERISA or the plan terms.<sup>77</sup> Furthermore, directed trustees are

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<sup>72</sup> For example, compliance and litigation costs. *Varity Corp. v. Howe*, 516 U.S. 489, 539 (1996) (Thomas, J., dissenting) (stating a holding in which an individual would be more likely to be held a fiduciary “could result in significantly increased liability, or at the very least heightened litigation costs, and an eventual reduction in plan benefits to accommodate those costs”).

<sup>73</sup> Because Presidents exert substantial control over agencies, some view agencies as agents of the President, as opposed to Congress. Nina A. Mendelson, *Agency Burrowing: Entrenching Policies and Personnel Before a New President Arrives*, 78 N.Y.U. L. REV. 557, 581–83 (2003). The public's support of a President through reelection, therefore, could be understood as support of the agencies that the President controls, and the agencies' policy preferences. On the other hand, an election of a President from a different party than the last may cause agencies to change policy. *See Motor Vehicle Mfrs. Ass'n of U.S. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 59 (1983) (Rehnquist, J., concurring in part and dissenting in part). After the reelection of President Obama, the Consumer Financial Protection Bureau announced that it may become involved in “helping” Americans manage their retirement savings, including 401(k) accounts. Carter Dougherty, *Retirement Savings Accounts Draw U.S. Consumer Bureau Attention*, BLOOMBERG (Jan. 18, 2013, 12:01 AM), <http://www.bloomberg.com/news/2013-01-18/retirement-savings-accounts-draw-u-s-consumer-bureau-attention.html> (“The bureau's core concern is that many Americans, notably those from the retiring Baby Boom generation, may fall prey to financial scams . . .”). A desire by the Bureau to help individuals avoid scams and manage savings accounts seems paternalistic, just as the Department's efforts to limit participant choice in directing investments is paternalistic.

<sup>74</sup> 29 U.S.C. § 1103(a) (2012).

<sup>75</sup> *Id.* (authorizing trustees to “manage and control assets of the plan”). Directed trustees might hold plan assets in custody, process contributions and investments, perform tax reporting, and furnish trust statements.

<sup>76</sup> Colleen E. Medill, *The Law of Directed Trustees Under ERISA: A Proposed Blueprint for the Federal Courts*, 61 MO. L. REV. 825, 826 (1996).

<sup>77</sup> 29 U.S.C. § 1102(b)(1). As this Section will describe, this requirement is fertile ground for litigation. If the direction is not consistent with ERISA, the directed trustee

fiduciaries with respect to the actions they take (or do not take) to follow the directions given to them.<sup>78</sup> Therefore, the question of which fiduciary duties a directed trustee will be held to have and thus be liable for is complex.

In response to Enron's pension plan litigation,<sup>79</sup> the Department of Labor issued a Field Assistance Bulletin<sup>80</sup> which attempted to clarify the duties of directed trustees.<sup>81</sup> The Bulletin acknowledged that the duties of a directed trustee are narrow, but stated that a directed trustee would have to question the prudence of transactions when the directed trustee possessed material non-public information that reflected negatively on a security held as an asset under the plan.<sup>82</sup> Furthermore, the Department adopted a mental culpability standard for liability, when the directed trustee "knows or should know" directions are contrary to the plan terms or ERISA.<sup>83</sup> This guidance has made it easier for

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cannot follow it. See *Employee Benefits and Executive Compensation Update—Fiduciary Duties of Directed Trustees*, SCHIFF HARDIN LLP (Mar. 4, 2005), [http://www.schiffhardin.com/File%20Library/Publications%20\(File%20Based\)/HTML/ebec\\_030405index.html](http://www.schiffhardin.com/File%20Library/Publications%20(File%20Based)/HTML/ebec_030405index.html).

<sup>78</sup> MEDILL, *supra* note 26, at 53 ("Although the functions of a directed trustee are narrowly circumscribed . . . in performing these functions the directed trustee nonetheless is a fiduciary."). If the participant's employer is insolvent, the directed trustee may be the only "deep pocket" the participant has a claim against. See *id.* at 500.

<sup>79</sup> *In re Enron Corp. Sec., Derivative & ERISA Litig.*, 284 F. Supp. 2d 511, 533, 535 n.11 (S.D. Tex. 2003). Enron's 401(k) plan included a program where the employer's matching contributions were automatically invested in company stock. A few months before Enron filed for bankruptcy, the company told its directed trustee to impose a lock down, effectively preventing the participants from selling Enron shares from their plan, even as the value of Enron's share fell dramatically. See also Jeffrey S. Klein & Nicholas J. Pappas, *Duties of Directed Trustees in ERISA Stock Drop Litigation*, N.Y. L.J., Oct. 9, 2007, [http://www.weil.com/wgm/cwgmhomep.nsf/Files/DutiesofDirectedTrusteesinERISA/\\$file/DutiesofDirectedTrusteesinERISA.pdf](http://www.weil.com/wgm/cwgmhomep.nsf/Files/DutiesofDirectedTrusteesinERISA/$file/DutiesofDirectedTrusteesinERISA.pdf).

<sup>80</sup> A Field Assistance Bulletin (FAB) is a type of "guidance document," which is defined as "an agency statement of general applicability and future effect, other than a regulatory action . . . that sets forth a policy on a statutory, regulatory or technical issue or an interpretation of a statutory or regulatory issue." Final Bulletin for Agency Good Guidance Practices, 72 Fed. Reg. 3432, 3434 (Office of Mgmt. & Budget Jan. 25, 2007); see also Donald J. Myers & Michael B. Richman, *Labor Department Issues Guidance on Fiduciary Responsibilities of Directed Trustees*, MARTINDALE.COM (Jan. 2005), [http://www.martindale.com/labor-employment-law/article\\_Reed-Smith-LLP\\_105634.htm](http://www.martindale.com/labor-employment-law/article_Reed-Smith-LLP_105634.htm) (explaining that a FAB is not binding law but would be considered persuasive authority representing the views of an agency).

<sup>81</sup> EMP. BENEFITS SEC. ADMIN., U.S. DEP'T OF LABOR, FIELD ASSISTANCE BULL. NO. 2004-03, FIDUCIARY RESPONSIBILITIES OF DIRECTED TRUSTEES (2004).

<sup>82</sup> *Id.* at 4–5. The Department reflected that directed trustees would not have to question the prudence of transactions when the directed trustee only had public information because, under the efficient market hypothesis, that information would already be impounded into the price of the security. *Id.*

<sup>83</sup> *Id.* at 3–4. Directed trustees can question certain transactions, discharging their duty by perhaps asking for a statement from the trustee's own ERISA attorney as to how the transaction fits with the plan or ERISA.

courts to dismiss claims of plaintiff-participants because the duty to question transactions is "significantly limited."<sup>84</sup>

However, the Department of Labor has seemed to reverse its position on the issue, at least with regard to transactions that involve the employer's own stock. Directed trustees are often involved in administering and executing transactions in defined contribution plans.<sup>85</sup> ERISA provides a safe harbor to fiduciaries that act pursuant to a decision made by a participant who exercised independent and informed choice.<sup>86</sup> However, the Department has written amicus briefs to challenge the position that the purchase of employer stock pursuant to the participant's discretion would avail the directed trustee of this safe harbor.<sup>87</sup> The Department has established a pattern arguing against the presumption that the duty to question transactions involving the purchase of employer stock was narrow; instead, the duty to question transactions would apply in many more cases.<sup>88</sup> The Department's position is paternalistic in that it assumes employees cannot independently make the decision to buy employer stock.

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<sup>84</sup> *Id.* at 4; Klein & Pappas, *supra* note 79. There is virtually no criticism from the industry concerning this field assistance bulletin. See William J. Kilberg et al., *A Measured Approach: Employment and Labor Law During the George W. Bush Years*, 32 HARV. J.L. & PUB. POL'Y 997, 1007 (2009) (stating the field assistance bulletin is "sensible" and "facilitat[es] the continued provision of directed trustee services at a reasonable cost without unrealistic liabilities").

<sup>85</sup> See Klein & Pappas, *supra* note 79.

<sup>86</sup> 29 U.S.C. § 1104(c)(1)(A) (2012) (stating that fiduciaries are not responsible for losses which result from participants' exercise of control).

<sup>87</sup> Greg Daugherty, *Sixth Circuit Allows ERISA Section 404(c) Safe Harbor To Protect a 401(k) Plan's Directed Trustee from Responsibility for Losses in Self-directed Brokerage Accounts*, EMP. BENEFITS L. REP. (July 14, 2011), <http://www.employeebenefitslawreport.com/2011/07/sixthcircuit-allows-erisa-section-404c-safe-harbor-to-protect-a-401k-plans-directed-trustee-from-responsibility-for-losses-in-self-directed-brokerage-accounts/>; see, e.g., Brief of the Sec'y of Labor, Hilda Solis, as Amicus Curiae Supporting Plaintiff-Cross-Appellee at 11–12, *Taylor v. KeyCorp*, 680 F.3d 609 (6th Cir. 2012) (Nos. 10-4163, 10-4198); Brief of the Sec'y of Labor, Elaine L. Chao, as Amicus Curiae Supporting Appellants and Requesting Reversal, *Tullis v. UMB Bank, N.A.*, 423 F. App'x 567 (6th Cir. 2011) (Nos. 06-4632, 06-4633).

<sup>88</sup> See Robert Steyer, *Critics Claim DOL Using Amicus Briefs To Steer by Pension Roadblocks*, PI ONLINE (July 25, 2011), [www.pionline.com/article/20110725/PRINTSUB/110729948](http://www.pionline.com/article/20110725/PRINTSUB/110729948) ("DOL's actions in recent years illustrate the department's conscious efforts to reverse established policy through amicus briefs . . . . DOL has been trying to make policy in the courts because they don't have much traction on this point in legislation or regulation." (internal quotation marks omitted)). Many federal circuits have adopted a presumption of prudence in the purchase of employer stock as set forth in an earlier case, *Moench v. Robertson*. Jose Martin Jara, *What Is the Correct Standard of Prudence in Employer Stock Cases?*, 45 J. MARSHALL L. REV. 541, 561 (2012) (citing *Moench v. Robertson*, 62 F.3d 553, 568 (3d Cir. 1995)). Yet, the Supreme Court will review the issue of whether purchases of employer stock are prudent. Lyle Denniston, *Court Grants Two New Cases*, SCOTUSBLOG (Dec. 13, 2013), <http://www.scotusblog.com/2013/12/court-grants-two-cases-8/>.

The Department of Labor's recent positions in the amicus briefs would, if accepted, make it easier for plaintiffs to state a claim for fiduciary breach.<sup>89</sup> Therefore, they represent an attempt by the Department of Labor to expand liability under ERISA. If directed trustees were to face expanded liability, they would increase service prices and thereby reduce employees' investment returns,<sup>90</sup> or possibly would leave the ERISA industry.<sup>91</sup> But institutional directed trustees serve the market by providing an efficient structure for the investment and safe guarding of plan assets. If the services become more expensive, or if service providers were to leave the industry, employees in defined contribution plans would have less opportunity to cost-effectively invest their plan accounts assets in securities markets.

### B. Broadening the Definition of Fiduciary Advice

The Department of Labor has tried and thus far failed to broaden its fiduciary advice definition. The Department previously adopted a five-factor regulatory test to determine whether a person had given investment advice for a fee and would thus be a fiduciary.<sup>92</sup> Recently, the Department noted that plan sponsors and participants often use consultants and advisers to help navigate the diverse array of choices offered through defined contribution plans.<sup>93</sup> They might also act as brokers to participants directing their 401(k) or IRA options. According to the Department, the consultants and advisers could give conflicted advice to cause self-dealing transactions,<sup>94</sup> but would escape liability because they would not be fiduciaries under the five-factor test.<sup>95</sup>

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<sup>89</sup> See Marcia S. Wagner, *Review of DOL Amicus Filings*, WAGNER L. GROUP (Aug. 2011), [www.erisa-lawyers.com/documents/401kAdvisor82911.pdf](http://www.erisa-lawyers.com/documents/401kAdvisor82911.pdf).

<sup>90</sup> Medill, *supra* note 76, at 863 ("Quite simply, if directed trustees are required to assume the full range of fiduciary responsibility and liability associated with the duty of independent inquiry, they must increase the price of their services accordingly.").

<sup>91</sup> See Definition of the Term "Fiduciary," 75 Fed. Reg. 65,263, 65,274 (proposed Oct. 22, 2010) (noting that service providers labeled as fiduciaries might "limit or discontinue the availability of their services or products to ERISA plans").

<sup>92</sup> The factors are that the advice must concern the value of investments or property; the advice must be provided on a regular basis; the advice must be given pursuant to a mutual agreement with respect to a plan; the advice must serve as the primary basis for investment decisions; and the advice must be individualized with respect to the particular needs of the plan. 29 C.F.R. § 2510.3-21 (2013).

<sup>93</sup> Definition of the Term "Fiduciary," 75 Fed. Reg. at 65,265.

<sup>94</sup> *Id.* (stating that plan fiduciaries might expect consultants to be impartial, but consultants can engage in conflicted transactions); Elizabeth MacBride, *A Q&A with Phyllis Borzi, the DoL Powerbroker Aiming To Remake the Retirement Market*, RIA BIZ (Mar. 3, 2011), <http://www.riabiz.com/a/5857389/a-qa-phyllis-borzi-the-dol-powerbroker-aiming-to-remake-the-retirement-market> (stating regulation was proposed so that "people aren't being steered to one product or another because of a financial interest (on the part of the person giving them the advice)").

<sup>95</sup> Definition of the Term "Fiduciary," 75 Fed. Reg. at 65,265; see also Marcus Baram, *Proposal To Protect Retirees' Nest Eggs Becomes Latest Lobbying Flashpoint*, HUFFINGTON

To address the issue, the Department proposed a regulation in 2010 that would have extended a new definition of investment advice.<sup>96</sup> Under the proposed regulation, consultants and other service providers would be deemed to provide fiduciary advice if they either made appraisals or fairness opinions about the value of securities, recommendations on investing, or recommendations as to the management of securities and also either represented themselves as acting as fiduciaries, were already fiduciaries, were investment advisers under the Investment Advisers Act of 1940, or provided advice pursuant to an agreement to provide advice in connection with the investment or management decisions of an ERISA plan.<sup>97</sup> The proposed regulation would have significantly expanded the field of persons considered fiduciaries.<sup>98</sup>

The announcement of this regulation was met with considerable controversy. The Department received more than 260 written public comments, including vigorous dissent from the business community and bipartisan members of Congress.<sup>99</sup> Much of the criticism dealt with the possibility of the proposed regulation causing increased costs for providing investment advice to participants, which would cause firms to leave the business.<sup>100</sup> The Department

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POST (June 14, 2011), [http://www.huffingtonpost.com/2011/06/14/retirementproposal\\_n\\_876343.html?id=1420](http://www.huffingtonpost.com/2011/06/14/retirementproposal_n_876343.html?id=1420) (“[T]he [original] rule required that advice be given on a regular basis for an adviser to be considered a fiduciary—so even if a retiree made a decision based on a single conversation, that infrequency exempted the adviser from the responsibility of being a fiduciary.”).

<sup>96</sup> Definition of the Term “Fiduciary,” 75 Fed. Reg. at 65,265.

<sup>97</sup> EMP. BENEFITS SEC. ADMIN., *supra* note 66, at 2.

<sup>98</sup> Paul Borden, *Proposed ERISA Regulations Defining Fiduciary To Be Withdrawn and Modified*, MORRISON FOERSTER (Sept. 26, 2011), <http://www.mofo.com/files/Uploads/Images/110926-Proposed-ERISA-Regulations.pdf>.

<sup>99</sup> Laura Miller Andrew et al., *DOL Withdraws Its Proposed Definition of ERISA Fiduciary*, SMITH GAMBRELL & RUSSELL LLP (Sept. 19, 2011), [http://www.sgrlaw.com/resources/client\\_alerts/1700/](http://www.sgrlaw.com/resources/client_alerts/1700/); Baram, *supra* note 95. A group of Democratic senators, including Max Baucus, Tom Harkin, and Claire McCaskill, expressed concern that the proposed regulation would “increas[e] administration costs.” Letter from Tom Harkin et al., Sens., U.S., to Hilda Solis, Sec’y, U.S. Dep’t. of Labor et al. (May 3, 2011). A group of Republican senators, including Kelly Ayotte and Scott Brown, warned that the regulation would increase the cost of providing investment services and reduce the number of businesses offering pensions. Letter from Susan M. Collins et al., Sens., U.S., to Hilda Solis, Sec’y, U.S. Dep’t of Labor (May 19, 2011).

<sup>100</sup> See, e.g., Donald J. Myers & Michael B. Richmond, *DOL Proposes Significant Changes to “Investment Advice” Fiduciary Definition*, MORGAN LEWIS 6 (Nov. 1, 2010), [http://www.morganlewis.com/pubs/EB\\_LF\\_SignificantChangesStatusDefinition\\_1\\_01nov20101.pdf](http://www.morganlewis.com/pubs/EB_LF_SignificantChangesStatusDefinition_1_01nov20101.pdf); Letter from Timothy E. Keehan, Vice President, Am. Bankers Ass’n, to Robert J. Doyle, Dir., Office of Regulations & Interpretations, Emp. Benefits Sec. Admin. 1 (Feb. 3, 2010); Letter from Barney Frank, Sen., U.S., to Hilda Solis, Sec’y, U.S. Dep’t. of Labor (Sept. 15, 2011) (stating that it is important to regulate in a manner that does not have “adverse effects on the choices available to consumers”); see also *Definition of Fiduciary Investment Advice: Hearing Before the Dep’t of Labor Emp. Benefits Sec. Admin.*, 112th Cong. 19–20 (2011) (statement of Linda E. Carlisle, General Counsel, Employee-Owned S-Corporations of America); Letter from Richard M. Whiting, Exec. Dir., Fin. Servs.



acknowledged that for some service providers, the costs of remaining in the market would outweigh the benefits.<sup>101</sup> Furthermore, the regulation may have covered attorneys, accountants, and other professionals giving advice, even if the advice did not concern the value of a particular investment or carry any potential for self-dealing.<sup>102</sup> The expansion of fiduciary duty was a paternalistic idea because it assumed that employees could not wisely direct their investments while dealing with service providers. Assistant Secretary of Labor Borzi defended the proposal by stating, "The world has gotten way too complicated for people to be able to make all those choices on their own."<sup>103</sup> After the comment process ended, the proposal was withdrawn.<sup>104</sup> However, the Department is planning to reintroduce the proposal.<sup>105</sup>

If the regulation had been enacted, consultants and other service providers would have faced expanded liability and the need to charge higher fees because they would have been more likely to have been held to be fiduciaries. With expanded liability, some might have left the ERISA industry. If these service providers did leave the market, employees would have had less assistance in directing their investment choices in defined contribution plans.

### *C. Monitoring and Disclosure of Options in Self-directed Brokerage Windows*

One aspect of many defined contribution plans is that many employers provide a broad, almost unlimited, choice of investments through brokerage firms such as Schwab or Fidelity, in addition to a core group of investment options that the employer selects or designates.<sup>106</sup> A product that allows

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Roundtable, to Office of Regulations & Interpretations, Emp. Benefits Sec. Admin. 6 (Feb. 3, 2011) (stating that if the regulation was to go in force, only participants who could receive independent investment advice would receive it).

<sup>101</sup> Definition of the Term "Fiduciary," 75 Fed. Reg. 65,263, 65,275 (proposed Oct. 22, 2010). But the Department argued the benefit of the regulation would outweigh the cost of some service providers' leaving the market. *Id.*

<sup>102</sup> See Letter from Matthew L. Eilenberg, Chair, Comm. on Emp. Benefits & Exec. Comp., N.Y.C. Bar, to Office of Regulations & Interpretations, Emp. Benefits Sec. Admin. 8-9 (Jan. 28, 2011) (stating attorneys' advice as to the legality of a certain transaction could fall under the regulation's definition of fiduciary advice); Letter from Mark. J. Ugoretz, President, ERISA Indus. Comm., to Office of Regulations & Interpretations, Emp. Benefits Sec. Admin. 3 (Feb. 2, 2011) (claiming regulation should include a safe harbor for attorney advice if attorneys make clear they do not intend to provide investment advice).

<sup>103</sup> MacBride, *supra* note 94.

<sup>104</sup> See Andrew et al., *supra* note 99.

<sup>105</sup> Press Release, Emp. Benefits Sec. Admin., US Labor Department's EBSA To Re-propose Rule on Definition of a Fiduciary (2011), available at <http://www.dol.gov/ebsa/newsroom/2011/11-1382-NAT.html>; Rebecca Moore, *House Approves Bill To Delay DOL Fiduciary Rule*, PLAN SPONSOR (Oct. 31, 2013), [http://www.plansponsor.com/House\\_Approves\\_Bill\\_to\\_Delay\\_DOL\\_Fiduciary\\_Rule.aspx](http://www.plansponsor.com/House_Approves_Bill_to_Delay_DOL_Fiduciary_Rule.aspx).

<sup>106</sup> There could be tens of thousands of investments available. See Letter from Lynn Dudley, Senior Vice President, Am. Benefits Council, to Phyllis Borzi, Assistant Sec'y,

participants to select investments beyond those that are designated as available under the plan is called a “brokerage window.”<sup>107</sup> The purpose of the brokerage windows is to allow participants to pick their own investments if they are not pleased with designated investment options.<sup>108</sup> Currently, plan sponsors have fiduciary duties with regard to designated investment options, including a duty to disclose information about the option to participants<sup>109</sup> and monitor the options to make sure that they are prudent.<sup>110</sup>

In 2012, the Department of Labor released a field assistance bulletin that expressed a view that would have extended monitoring and disclosure obligations to investments in the brokerage window if significant numbers of participants chose them.<sup>111</sup> Essentially, some brokerage window investments would be treated the same way as designated investments.<sup>112</sup> These obligations would have necessarily involved a duty to discover which choices participants were making in the brokerage window in order to establish whether a “significant number” invested in these options, triggering increased fiduciary obligations.<sup>113</sup>

Criticism of the Department’s position came in two forms. First, the broadening of fiduciary duties with respect to brokerage windows may have raised “novel legal or policy issues”<sup>114</sup> and therefore triggered requirements for

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Emp. Benefits Sec. Admin. 2 (June 14, 2012). Nearly thirty percent of defined contribution plans offer this option. Lisa Shidler, *New DOL Rule Effectively Kills Off Open Architecture Option Favored by Some Big Plan Participants—And Sets Off the 401(k) Industry*, RIA BIZ (June 19, 2012), <http://www.riabiz.com/a/13897002/new-dol-rule-effectively-kills-off-open-architecture-option-favored-by-some-big-plan-participants---and-sets-off-the-401k-industry>.

<sup>107</sup> 29 C.F.R. § 2550.404a-5(h)(4) (2013).

<sup>108</sup> Shidler, *supra* note 106.

<sup>109</sup> 29 C.F.R. § 2550.404a-5(c)-(d) (information that must be disclosed includes how the participant can control investment, information about expenses relating to the plan, and financial statements).

<sup>110</sup> See *Pfeil v. State St. Bank & Trust Co.*, 671 F.3d 585, 597, 600 (6th Cir. 2012) (citing 29 C.F.R. § 2550.404c-1(d)(2)(iv)); see also *id.* at 600 (“[T]he 404(c) regulation also provides that the safe harbor provision ‘does not serve to relieve a fiduciary from its duty to prudently select and monitor any service provider or designated investment alternative offered . . . .’” (emphasis added)); *Howell v. Motorola, Inc.*, 633 F.3d 552, 567 (7th Cir. 2011) (“[T]he selection of plan investment options and the decision to continue offering a particular investment vehicle are acts to which fiduciary duty attach . . .”).

<sup>111</sup> EMP. BENEFIT SEC. ADMIN., U.S. DEP’T OF LABOR, FIELD ASSISTANCE BULL. NO. 2012-02, at 19 (2012). The guidance from the Department was specified in a question and answer format. See *id.* at 2-23.

<sup>112</sup> Shidler, *supra* note 106.

<sup>113</sup> Laura Miller Andrew et al., *DOL Fiduciary Alert: 401(k) Plan Brokerage Windows*, SMITH GAMBRELL & RUSSELL LLP (June 19, 2012), [http://www.sgrlaw.com/resources/client\\_alerts/1941/](http://www.sgrlaw.com/resources/client_alerts/1941/) (recommending that plan sponsors contact their investment advisers to review which investment options their participants are choosing).

<sup>114</sup> Letter from Dudley, *supra* note 106, at 6.

the Department to solicit public comments,<sup>115</sup> a procedure it did not undertake.<sup>116</sup> More importantly, there was concern that the cost of and pragmatic difficulty with respect to disclosing information about and monitoring the prudence of every investment option in the brokerage window would be unfeasible.<sup>117</sup> With the increased cost and fiduciary oversight responsibility, many employers may have liquidated their participants' self-directed brokerage window accounts.<sup>118</sup> Therefore, the choices of participants would ultimately have been reduced, which is in line with a paternalistic framework. The Department ultimately rescinded its position in a new field assistance bulletin, but stated it may explore further change through "amendment[]" of regulatory provisions."<sup>119</sup>

#### IV. THE DEPARTMENT OF LABOR'S ACTIONS CONFORM TO A PATERNALISTIC MODEL AND WILL NOT WORK

The actions of the Department of Labor<sup>120</sup> would have the impact of limiting participants' choices in the context of defined contribution plans. These services—those of a directed trustee facilitating access to the securities markets, of consultants that provide access to investment services to assist participants in making investment decisions, and of self-directed brokerage windows that provide broad choices of investments—all have a bearing on a primary feature of defined contribution plans: participant choice or direction. By trying to ratchet up fiduciary duty in these realms, the Department would have expanded possible liability and increased the cost of performing these services. Some firms would have left the market. Therefore, participant choice would have been

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<sup>115</sup> See Final Bulletin for Agency Good Guidance Practice, 72 Fed. Reg. 3432, 3440 (Office of Mgmt. & Budget Jan. 25, 2007) (requiring agencies to allow public comments for significant guidance documents). The Office of Management and Budget defines a "significant guidance document" as a guidance document that "may reasonably be anticipated" to "[r]aise novel legal or policy issues." *Id.* at 3434. Further, if the guidance document is "economically significant," the agency must respond to the comments. *Id.* at 3440; see also Christopher E. Wilson, Comment, *Not Good Enough for Government Work: How OMB's Good Guidance Practices May Unintentionally Complicate Administrative Law*, 59 ADMIN. L. REV. 177, 186 (2007).

<sup>116</sup> See Letter from Dudley, *supra* note 106, at 6.

<sup>117</sup> *Id.* at 3 (stating that having to monitor brokerage windows and modify existing disclosure processes would "trigger[] enormous costs"); Letter from Am. Bankers Ass'n et al., to Phyllis Borzi, Assistant Sec'y, Emp. Benefits Sec. Admin. 5 (June 25, 2012) ("[T]he disclosures required for the first time by [the Department Field Assistance Bulletin] will involve significant and costly manual processes . . ."); Shidler, *supra* note 106 ("It's lunacy to consider that self-directed brokerage accounts should be supervised by advisors.").

<sup>118</sup> Letter from Dudley, *supra* note 106, at 4; Letter from John F. Kerry, Sen., U.S., to Hilda Solis, Sec'y, U.S. Dep't. of Labor 1–2 (July 24, 2012).

<sup>119</sup> EMP. BENEFITS SEC. ADMIN., U.S. DEP'T OF LABOR, FIELD ASSISTANCE BULL. NO. 2012-02R, at A.39 (2012).

<sup>120</sup> See *supra* Part III.

reduced. The Department's attempts conform to a paternalistic model of how retirement savings plans should work. This approach is functionally problematic because the attempts have not produced any changes in the law and normatively problematic because less choice will not help participants unless employers or other service providers agree to assume the risk of the investments, which they cannot do and will not do in a defined contribution framework.

### A. *Explanation of the Paternalistic Model*

There are two competing models for pension plan operation. They differ in the level of participant control offered to either employees or employers over investments in the plan. A defined benefit pension plan represents what is meant by a "paternalistic model."<sup>121</sup> The defined benefit plan is paternalistic because the employer makes decisions on behalf of workers and assumes funding obligations as well as the risk of providing defined retirement benefits when these are required.<sup>122</sup> On the other hand is the "individual responsibility model," best exemplified by a type of defined contribution plan: the 401(k).<sup>123</sup> The 401(k) plan fits within an individual responsibility model because the employees are responsible for funding and directing investment choices and bear the risk of providing for their own retirement security. Pension plans exist on a continuum between complete paternalism and complete individual responsibility, with the difference being the level of participant control.

Professor Stabile has proposed reforming 401(k) plans by decreasing their individual responsibility aspect and increasing paternalism.<sup>124</sup> The idea is that many participants are financially illiterate and cannot be easily taught how to invest well.<sup>125</sup> Furthermore, this proposal argues that when given options in the 401(k), participants cannot exercise them effectively for two reasons. First, plan sponsors or employers might have the potential to steer participants into certain choices, which may not be the best, by framing investment options.<sup>126</sup> Second, participants cannot make prudent, wise decisions about saving for retirement because the perspective of a young employee with respect to saving for

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<sup>121</sup> MEDILL, *supra* note 26, at 122.

<sup>122</sup> *Id.*

<sup>123</sup> *Id.* Different types of defined contribution plans may feature different levels of individual responsibility. For example, in a profit sharing plan, employers may provide the funds for the employer's individual account.

<sup>124</sup> See Stabile, *supra* note 61, at 517; Susan J. Stabile, *Freedom To Choose Unwisely: Congress' Misguided Decision To Leave 401(k) Plan Participants to Their Own Devices*, 11 CORNELL J.L. & PUB. POL'Y 361, 391 (2002); Susan J. Stabile, *The Behavior of Defined Contribution Plan Participants*, 77 N.Y.U. L. REV. 71, 71 (2002).

<sup>125</sup> See Stabile, *supra* note 61, at 504 (stating that employees want to be told how to invest, not to be shown how to make decisions).

<sup>126</sup> See Stabile, *Freedom*, *supra* note 124, at 378-81 (explaining framing concept by positing that when presented with a choice between a small and large radio, consumers would choose the smaller, but when represented with a choice between small, medium, and large radios, consumers would choose the medium-sized radio).

retirement is vastly different from that of a retiree.<sup>127</sup> This argument concludes that participant direction—and individual responsibility—is a problem.<sup>128</sup>

## B. Criticism of the Paternalistic Model and the Department of Labor

### 1. Paternalism in Defined Contribution Plans Is Theoretically Unsound

The notion that employees intrinsically cannot make investment decisions for themselves, and therefore should not be allowed to make those decisions, is problematic. Why should we want to teach children basic financial skills and the importance of saving if we assume that adults cannot make decisions necessary to their retirement security? Society has used education to help individuals navigate complex systems for generations. For example, Rousseau argued that education is a process by which society can be improved, and government will become more responsive to the people.<sup>129</sup> The Founding Fathers also recognized education as playing an important role in defending democracy against tyranny.<sup>130</sup>

Professor Stabile identified two situations where participants may not exercise choice effectively,<sup>131</sup> but there is no reason to believe that after obtaining an investment education, participants' choices would not improve. An employer framing investment choices in a specific manner may alter the outcome of a choice.<sup>132</sup> However, the result may be different when the participants are knowledgeable about the subject of the choice. For example, participants presented with a choice between a small and large product may change their views about the products when they are instead presented with a small, medium, and large product.<sup>133</sup> However, if participants were educated

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<sup>127</sup> Young participants are less likely to understand the importance of saving for retirement. *See id.* at 388–90 (analogizing young participants to incompetents who should not be able to make their own medical decisions).

<sup>128</sup> Stabile suggests that ERISA's safe harbor for fiduciaries from the imprudent directions of participants, established in 29 U.S.C. § 1104(c), might be eliminated. *See id.* at 397. With the threat of potential liability for the imprudent acts of its participants, employers would eliminate the ability of participants to direct investments. *Id.* at 398.

<sup>129</sup> *See* Frederick William Dame, *Jean-Jacques Rousseau's Views on Adult Education*, 42 INT'L REV. EDUCATION 205, 222 (1996).

<sup>130</sup> *See, e.g.,* Letter from John Madison to William Taylor Barry (Aug. 4, 1822) ("Learned institutions . . . throw that light over the public mind which is the best security against crafty & dangerous encroachments on the public liberty.").

<sup>131</sup> *See supra* notes 126–127 and accompanying text.

<sup>132</sup> Stabile, *Freedom*, *supra* note 124, at 386–91.

<sup>133</sup> *See id.* at 378–79. Some of the parameters relevant to participant direction of pension plans would concern asset allocation of the funds in the participant's account, which would depend on an individual's time horizon and risk tolerance, although diversification is also important. U.S. SEC. & EXCH. COMM'N, BEGINNER'S GUIDE TO ASSET ALLOCATION, DIVERSIFICATION, AND REBALANCING (2009), available at <http://www.sec.gov/investor/pubs/assetallocation.htm>. These factors can seem overwhelming to participants who are faced with many options, such as in the open brokerage window, but financial education can

about the parameters of the products, as well as the pros and cons about different features, their choice may not be context-dependent. In addition, while it may be true that young participants could be expected by default to not have the perspective of older participants near retirement,<sup>134</sup> with education about the need to save for retirement and the power of the time-value of money, the participants' behavior while young may change.

Adherents to the paternalistic framework propose to shift defined contribution plans that feature individual responsibility like the 401(k) closer to the model of a defined benefit plan which features paternalism. Functionally, the defined benefit paradigm is becoming a dead letter (we have been moving away from it for years).<sup>135</sup> One of the major reasons for the decline in defined benefit plans is cost.<sup>136</sup> It has been argued that by shifting the liability for bad outcomes from participants to employers, employers will try to reduce cost by reducing participant direction, so that they will not become responsible for the bad choices of participants.<sup>137</sup> But if employers are directing investments on behalf of employees, then employers would not be able to access the safe harbor that provides protection from liability for the choices made by participants, and costs would increase.<sup>138</sup> Some employers would cancel their pension rather than face any increased cost.<sup>139</sup> For those participants, with no pension plan, the goal of retirement security would be lost. Why risk such a catastrophic outcome?

## 2. *The Department of Labor's Actions Imply a Paternalistic Outlook*

The Department of Labor's behavior fits the paternalistic model because the idea of making directed trustees, service providers, and employers more accountable than they currently are under ERISA assumes that employees are unable to protect themselves. Businesses will offer fewer options to employees when their accountability through fiduciary duty increases.<sup>140</sup> The duty to monitor every investment in the self-directed brokerage window illustrates the problem, because there are more options in these plans' brokerage windows than can be practically evaluated.<sup>141</sup> The only real solution in the face of that

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assist them. MEDILL, *supra* note 26, at 490 (citing ALICIA H. MUNNEL & ANNIKA SUDEN, COMING UP SHORT 65 (2004)).

<sup>134</sup> See Stabile, *Freedom*, *supra* note 124, at 378–86.

<sup>135</sup> Papa, *supra* note 66, at 377 (“Employers are increasingly replacing defined benefit plans with 401(k) plans, leaving workers responsible for paying part of the cost of their retirement and for managing their own retirement investments.”).

<sup>136</sup> See Stabile, *supra* note 61, at 496–97.

<sup>137</sup> See Stabile, *Freedom*, *supra* note 124, at 398.

<sup>138</sup> See 29 U.S.C. § 1104(c)(1)(A) (2012); see also *Varity Corp. v. Howe*, 516 U.S. 489, 539 (1996) (Thomas, J., dissenting).

<sup>139</sup> See, e.g., Letter from Dudley, *supra* note 106, at 5.

<sup>140</sup> This process may include the liquidation of current investment options. *Id.* at 3.

<sup>141</sup> See *id.* at 2 (noting that there could be tens of thousands of investments available in self-directed brokerage windows).

regulation would have been to limit the number of options to a manageable number, decreasing the number of investment options available to employees.

One problem with simply increasing the responsibility of plan sponsors and other fiduciaries, as the Department of Labor has advocated, is that shifting the risk away from employees only works well in the defined benefit paradigm. Under that level of paternalism, benefit plans are insured. The Pension Benefit Guaranty Corporation operates as a form of insurance, taking over the funding and management of defined benefit plans in serious arrears.<sup>142</sup> Within the defined contribution framework, it would be virtually impossible for investment insurance companies to gauge the risk of the countless investment decisions that employees may make. Therefore, an insurance product would be either unavailable or extremely expensive.

Increasing fiduciary duties to incentivize a paternalistic framework would not completely eliminate the risk of bad actors. There would only be deterrence. Limiting choices actually might lead to another Enron-type situation where all of the employees' money goes into a single pot that is not worth investing in, or is very speculative and risky, and then the pot goes bankrupt. In a paternalistic plan, a fiduciary would have the power to direct all employees to bad investments. Even if liable for fiduciary breach, in bankruptcy or insolvency, those responsible would be without any assets with which to make employees whole. For instance, even though Bernie Madoff is liable for his malfeasance, not everyone who invested with him will ultimately be made whole.<sup>143</sup>

Employers and other fiduciaries that have small levels of assets would be responsible to make whole the losses of the imprudent investments of their employees, but would not actually have enough assets to do so. That is why some propose to adopt a Pension Benefit Guaranty Corporation that covers all plans, not only defined benefit plans. However, this proposal would require immense levels of funding,<sup>144</sup> including premiums from employers, and it is not something that the Department of Labor has the power to do.<sup>145</sup>

The business community's lobbying efforts and congressional action<sup>146</sup> have dampened the Department of Labor's plans to expand regulatory requirements. The Department will likely continue to be ineffectual in the future with regards to this matter. Nevertheless, the Department may continue on its

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<sup>142</sup> See Allen & Bales, *supra* note 19, at 456.

<sup>143</sup> See Erik Larson, *Madoff Trustee Tops \$10 Billion Recovery with Bank Deal*, BLOOMBERG (Jan. 8, 2014), <http://www.bloomberg.com/news/2014-01-07/madoff-trustee-to-get-543-million-in-jpmorgan-accord.html>.

<sup>144</sup> Although the Pension Benefit Guaranty Corporation only covers defined benefits and collects premiums from the sponsors of all defined benefit plans, it was already in a deficit of \$21.9 billion by the end of 2009. PENSION BENEFIT GUAR. CORP., ANN. REP. 2009, at 2 (2009).

<sup>145</sup> The scope of the Pension Benefit Guaranty Corporation does not allow the Department of Labor to extend coverage in such a manner. See 29 U.S.C. § 1302(b) (2012).

<sup>146</sup> See, e.g., *supra* notes 99, 105, & 117–118 (cataloguing pressure on the Department of Labor from the business community and members of Congress).

path because the reelection of President Barack Obama will not alter its staffing. The Department should focus its time instead on efforts that are reasonably calculated to produce an actual positive change in the system. Some companies may choose to offer a paternalistic pension plan.<sup>147</sup> Essentially, that should be a choice between management of a company and its employees, not one imposed by the government.

#### V. PROPOSALS FOR INCREASED EDUCATION AND LIMITED DUTY FOR EFFORTS TO EDUCATE AND ADVISE EMPLOYEES IN MAKING DECISIONS

The goal of retirement security would best be furthered by enhancing the financial literacy of employees. Employees tend to make better decisions after being educated.<sup>148</sup> But many employees often fail basic financial knowledge tests.<sup>149</sup> ERISA has taken some strides in providing investment education, but the law can make it easier for employers to offer it or directly incentivize it.

Others have called for education as a requirement or duty.<sup>150</sup> Although the proponents have identified some elements of a curriculum (like the importance of diversification), it would be problematic to develop the contours of this duty. Do employers need to contract with third-party financial educators or can they undertake education by themselves? If employers use third parties to educate their employees, would the duty shift to the third parties? Could there be a breach if employees concede they received information, but claim it did not convince them to make prudent decisions, such as diversification, or they did not understand it? It may take case law to answer many of these questions and

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<sup>147</sup> Carolyn Bigda, *A New Type of 401(k): No Fund Picking Allowed*, CNN MONEY (Oct. 30, 2012), <http://money.cnn.com/2012/11/01/retirement/managed-401k-plans.moneymag/index.html?iid=obnetwork>.

<sup>148</sup> See MEDILL, *supra* note 26, at 490 (arguing that investment education can counter psychological biases, such as high information cost); Medill, *supra* note 64, at 24–25 (stating many employees change their directed investment allocations after reading education materials); Jayne E. Zanglein, *Investment Without Education: The Disparate Impact on Women and Minorities in Self-directed Defined Contribution Plans*, 5 EMP. RTS. & EMP. POL'Y J. 223, 245–46 (2001) (citing a study that found individuals who had greater levels of financial education saved more for retirement); Noah Smith, *How To Fix America's Wealth Inequality: Teach Americans To Be Cheap*, ATLANTIC (Mar. 12, 2013, 9:19 AM), <http://www.theatlantic.com/business/archive/2013/03/how-to-fix-americas-wealthinequality-teach-americans-to-be-cheap/273940/> (stating that financial education can help individuals avoid pension funds that charge overly high fees that reduce investment returns).

<sup>149</sup> See Annamaria Lusardi et al., *Financial Literacy Among the Young: Evidence and Implications for Consumer Policy* 3 (Nat'l Bureau of Econ. Research, Working Paper No. 15352, 2009) (finding only twenty-seven percent of young people understand compound interest, inflation, and diversification); see also Medill, *supra* note 64, at 15–17 (stating most employees do not calculate how much they need for retirement and cannot distinguish the characteristics of different investment vehicles, such as mutual funds and certificates of deposit).

<sup>150</sup> Papa, *supra* note 66, at 401–05 (arguing in favor of mandatory education for employees that would assist them in setting a savings goal and reaching it).



develop appropriate interpretation. In the meantime, employers would be in an uncomfortable situation, awaiting litigation that might disincentivize their provision of pension plans. The law needs to incentivize provision of pension plans.

As part of the Pension Protection Act of 2006, the Department of Labor was directed to make available information on investing and diversification.<sup>151</sup> Congress had previously told the Department to maintain a program to promote outreach to the public on retirement savings.<sup>152</sup> The Department has responded by creating some educational materials, which are posted on a website.<sup>153</sup> Congress should consider amending the reporting and disclosure sections of ERISA to require employers to provide the information that the Department has created. Although employees are currently provided with the URL in required disclosures, it is unlikely that participants navigate to the Department's website, even if they have an internet connection, if only due to the effort of having to do so. Participants would be more likely to read hard copy printed materials provided with other plan documents than navigate to a website. In addition, the cost of providing a thirty-page document to participants would be negligible for employers when compared to the amount of paper that is already required. But with its statutory authority, the Department could do much more to help provide investment education to participants.

#### *A. Adoption of Safe Harbors for Educational Activities*

Employers would be better served by the Department creating more investment education exemptions, to create realms where there would be no liability for employers to provide education. In 1996, the Department of Labor issued a regulation to incentivize educational activities.<sup>154</sup> The regulation creates certain "safe harbors"—specific types of activity that are not subject to fiduciary responsibility as "investment advice" because they deal with

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<sup>151</sup> See MEDILL, *supra* note 26, at 85.

<sup>152</sup> 29 U.S.C. § 1025(a)(2)(B)(ii) (2012) (requiring administrators of pension plans with individual accounts to furnish a statement that includes "an explanation, written in a manner calculated to be understood by the average plan participant, of the importance, for the long-term retirement security of participants and beneficiaries, of a well-balanced and diversified investment portfolio, including a statement of the risk that holding more than 20 percent of a portfolio in the security of one entity (such as employer securities) may not be adequately diversified").

<sup>153</sup> See *Investing and Diversification*, DEP'T LABOR, <http://www.dol.gov/ebsa/investing.html> (last visited Jan. 20, 2014).

<sup>154</sup> 29 C.F.R. § 2509.96-1(b) (2013) ("With both an increase in the number of participant-directed individual account plans and the number of investment options available to participants and beneficiaries under such plans, there has been an increasing recognition of the importance of providing participants and beneficiaries, whose investment decisions will directly affect their income at retirement, with information designed to assist them in making investment and retirement-related decisions . . .").

education.<sup>155</sup> However, the line between the provision of advice and education is still not clear.<sup>156</sup> The Department of Labor should spend its time trying to clarify and broaden the education exceptions to fiduciary duty instead of trying to find ways to broaden fiduciary duty.

One way the Department could help would be to create its own educational curriculum. It could train and certify educators who could go out and perform the task. EBSA already performs seminars to educate plan sponsors in major cities<sup>157</sup> and maintains a hotline to answer some legal questions from employees.<sup>158</sup> It could also provide educational sessions for employees. As a second option, the Department could also approve and pre-clear the curricula of third parties, who are in the business of providing investment services. The approval of curricula could function in a manner similar to permitting by the EPA or other agencies.<sup>159</sup> Those seeking permits to provide investment education in a safe harbor would have to submit documents to the Department providing information about the curriculum's details to ensure it would provide useful information, as defined by the Department. A third option would be for the Department to delegate this task to professional organizations that require prospective educators to undergo internal training or testing. This process would resemble the role of the Financial Industry Regulatory Authority, a non-governmental organization that administers the Series 7 test, which individuals are required to pass in order to sell securities.<sup>160</sup>

An employer's usage of these options would be a safe harbor or exception to fiduciary status. For example, the employer could hire a company or individual who has earned a permit of providing investment education—not advice—that will then present an education curriculum to employees. Perhaps this curriculum would be presented to employees during a company retreat or in the employer's workplace in a conference area.

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<sup>155</sup> 29 C.F.R. § 2509.96–1(d) (listing certain activities that would not constitute rendering investment advice).

<sup>156</sup> Dana M. Muir, *The Dichotomy Between Investment Advice and Investment Education: Is No Advice Really the Best Advice?*, 23 BERKELEY J. EMP. & LAB. L. 1, 20–22 (2002). If the employer provides too much information or even answers an employee's question, it may be considered as providing investment advice. *See id.* at 21.

<sup>157</sup> *Fiduciary Education Campaign*, DEP'T LABOR, <http://www.dol.gov/ebsa/fiduciaryeducation.html> (last visited Apr. 2, 2014).

<sup>158</sup> *Organizational Chart/Regional and District EBSA Offices*, DEP'T LABOR, [http://www.dol.gov/ebsa/aboutebsa/org\\_chart.html#mission](http://www.dol.gov/ebsa/aboutebsa/org_chart.html#mission) (last visited Apr. 2, 2014) (“EBSA’s Benefits Advisors responded to over 375,000 telephone, written and electronic inquiries and complaints from plan participants, employers and plan sponsors.”).

<sup>159</sup> *See, e.g., Frequently Asked Questions About Air Permits*, ENVTL. PROTECTION AGENCY, <http://www.epa.gov/region09/air/permit/pmfaq.html> (last visited Apr. 2, 2014) (requiring those seeking permits to produce air pollution to submit a plan for compliance with environmental law in the permit application).

<sup>160</sup> *Series 7 Examination*, U.S. SECURITY & EXCHANGE COMMISSION, <http://www.sec.gov/answers/series7.htm> (last visited Apr. 2, 2014).

Furthermore, while the Department's regulation contemplates the use of computer technology to administer investment education, it should be revamped to reflect today's technological possibilities. Under the Department of Labor's current position, computer programs that would otherwise qualify under the regulation may sometimes be described as providing investment advice, depending on who developed them.<sup>161</sup> To capture the true difference between advice and education, the Department of Labor should invite the submission of software products designed to educate employees about their investment options. The Department of Labor could certify or approve them as providing information that is sufficiently general or hypothetical so that is not to be considered investment advice. The current burden on seeking an exception to the advice rule is put on plan sponsors and service providers, but it should be put on software designers whose product, if sufficiently general, could be used by multiple plan sponsors for profit. Therefore, the provision of these programs to employees would also constitute a safe harbor from fiduciary liability. Employers could license the software for use by their employees to help them gain an understanding on how to effectively invest.

### B. Tax Deduction for Education Costs

Another idea to incentivize the growth of educational activity by employers would be to provide a deduction in the tax code for sums spent by an employer in the furtherance of these activities. The structure of the statute would follow other business deductions. But the deduction's spirit would be in line with the basic Internal Revenue Code provisions that provide for qualified pension plans. These provisions set out the requirements for the favorable tax treatment of pension plans and already allow employers to deduct funds spent in their funding.<sup>162</sup> The definition of just what furtherance of investment education means would include the safe harbors from fiduciary liability this Note has suggested above, such as hiring an accredited professional to present an investment education curriculum or licensing software for that purpose. The statute should also carry a mandate against discrimination in favor of highly compensated employees. The deduction would be capped to prevent irrational sums of money being spent in these activities, but it would be tied to the number of employees participating in the plan. This concept should not be new

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<sup>161</sup> There is no reason for the distinction, as those programs which would fall under the current safe harbor might be subject to a "steering problem" where they would suggest to employees that they use options that would produce for service providers the greatest fees. Medill, *supra* note 64, at 59–61.

<sup>162</sup> To be qualified for a deduction, a pension plan must meet the requirements of Internal Revenue Code Section 401(a). MEDILL, *supra* note 26, at 94. These requirements include limited nondiscrimination in terms of plan participation and benefit accrual among employees. *Id.* at 95 (stating code requirements were designed so as to "not disproportionately favor higher income employees"). Congress often changes the amount that can be deducted, but the limits can be found in Code Section 404. *Id.* at 191.

because the Internal Revenue Code provisions that govern qualified plans already limit tax-deductible contributions.

### *C. Possible Objections to Expanding the Role of Education*

#### *1. Employees Need Advice, Not Education*

Some critics might argue that participants would rather be told by advisers how to invest or have their investments made for them, rather than make the decisions for themselves. However, many participant-directed plans already allow employees to hire investment advisers to be paid with fees from their plans. If employees do not utilize this option, it may be because investment advice fees will reduce the amount of funds in their accounts. If employers were required to buy investment advice services for their employees, it may increase the costs of administering pension plans to prohibitive levels. In addition, because the selection of an investment adviser is discretionary, employers may face fiduciary liability in the event that employees face investment losses as a result of the adviser's activities.

Alternatively, a critic may argue that participants require advice because many pension service providers have already provided information about the investment options they offer. But education should include more than the provision of information. Participants need to be taught the skills to process available information to make choices suited to their own needs.

#### *2. The Federal Government Should Not Increase Subsidies in a Time of Massive Debt*

The federal government has enormous levels of debt.<sup>163</sup> This issue of the national debt and budget deficits has engendered uncertainty about the solvency of the United States and political gridlock. To allow a deduction for sums by employers spent on education would decrease revenue collected by the government. It would functionally be a subsidy. Some might argue that the general policy of the federal government should be to increase revenue collected, not to decrease it.

On the other hand, it is also a policy of the federal government to promote retirement security.<sup>164</sup> Social Security, one of the most massive government fiscal outlays, is designed to promote that purpose but may not succeed. ERISA

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<sup>163</sup> As of January 6, 2014, the total public debt outstanding was over \$17.3 trillion. BUREAU OF THE PUB. DEBT, U.S. DEP'T OF THE TREASURY, THE DEBT TO THE PENNY AND WHO HOLDS IT (2014), available at <http://www.treasurydirect.gov/NP/BPDLogin?application=np>. The United States has been running hundreds of billions in yearly budget deficits since 2002. OFFICE OF MGMT. & BUDGET, FISCAL YEAR 2013 HISTORICAL TABLES BUDGET OF THE U.S. GOVERNMENT 5-6, 22 (2012), available at <http://www.whitehouse.gov/sites/default/files/omb/budget/fy2013/assets/hist.pdf>.

<sup>164</sup> 29 U.S.C. § 1001(a) (2012).

too was enacted to promote retirement security. Currently, the deductions connected with pension plans constitute the third-largest tax expenditure, about \$100 billion a year.<sup>165</sup> Compared to that amount, a capped deduction for providing education to participants would be paltry. Furthermore, to increase investment education would clearly meet the policy of providing retirement security. Currently, a troublingly small number of Americans are thinking about retirement, putting aside funds for it, and are confident in their ability to invest. Yet, many Americans are in participant-directed plans that depend on their ability to make investment decisions. Something needs to be done to empower employees to make decisions that will provide them with adequate retirement security.

## VI. CONCLUSION

Currently, Americans are not saving enough for retirement. If left unchecked, this problem will lead to widespread elder poverty. Over thirty years ago, Congress enacted ERISA to help ensure retirement security by regulating private pension plans created by employers. Since then, the defined contribution plan, relying on the directions of employees to make investment decisions, has become the dominant form of pension plan. These plans put the risk of bad investment decisions on employees, not their employers. In other words, most pension plans today rely on individual responsibility, not paternalism.

In response, the Department of Labor is attempting to burden employers and pension plan service providers with increased levels of fiduciary duty. For example, the Department took the position in litigation that directed trustees must question the prudence of employees' decision to buy employer's stock in their plan. In addition, the Department proposed a fiduciary advice rule that would have expanded the field of service providers who would have been considered fiduciaries after providing investment information to employees. Finally, the Department stated that plan sponsors should have the fiduciary duties of monitoring and disclosure of multitudinous investment options in open brokerage windows.

If the Department succeeds on its path, it will force employers and service providers to spend more time overseeing employees' investment options. That goal is paternalistic because it assumes that employees cannot make these decisions for themselves. If employers and service providers do not meet these new proposed obligations, they will be more likely to be liable for losses on employees' plans. This paternalistic framework will increase the cost of providing and administering pension plans and ultimately may cause employers to stop providing plans and service providers to stop offering services altogether. ERISA neither requires employers to establish plans, nor does it

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<sup>165</sup> MEDILL, *supra* note 26, at 19 (citing JOINT COMM'N ON TAXATION, ESTIMATES OF FEDERAL TAX EXPENDITURES FOR FISCAL YEARS 2009–2013 (2010)).

require them to maintain them forever. If employers choose to end their plans, the goal of retirement security under ERISA will be lost.

To promote retirement security, the Department should assist in the provision of investment education, to empower employees to make decisions on their own behalf. For example, the Department should propose that if employers and plan sponsors follow specific safe harbors in providing investment education, they will not be held liable as providing investment advice. Moreover, Congress should directly incentivize the provision of investment education by providing a tax deduction for costs by employers spent in that regard. The current model of pension plan depends on employees making informed decisions to direct investments on their own behalf. Investment education will provide a vehicle for employees to exercise these decisions prudently, putting them on the road to a secure and comfortable retirement.